

ISA 240 Response from Audit Committee Chair 2017/2018

Fraud risk assessment

Auditor Question	Response
Have the Council and Pension Fund assessed the risk of material misstatement in the financial statements due to fraud?	<p>Yes.</p> <p>From the work that has come before the Audit Committee in the previous financial year, from officers, from SWAP as our internal auditors, and from previous Grant Thornton reports, I have a high level of confidence that this has been addressed in a number of ways.</p> <p>I note that your materiality levels this year are £15.1m for the County Council and £19.7m for the Pension Fund. There have been no audit reports that have been presented that have suggested that we are exposed to any fraud risks of this magnitude.</p> <p>Our general control environment around fraud controls has not changed from previous years, and I would consider that the following are relevant factors:-</p> <p>The Anti-Fraud and Corruption report that came to Audit Committee in January 2018, showed that officers had considered all the national trends in fraud, and that SWAP audits and other measures such as participation in the National Fraud Initiative are targeted against the greatest risks.</p> <p>I am aware that the work on the National Fraud Initiative has shown that our controls on Accounts Payable are already finding these potential issues and that these have already been resolved. We have a lot of confidence in our key systems such as Accounts Payable and Accounts Receivable. There are all the normal controls in our SAP Financial system that makes fraud less likely, such as division of duties around ordering and receiving of goods. Also, I am told that with our difficult financial position, only the most senior officers can approve orders for the higher cost orders, with anything over £25,000 needing to be signed off by a SLT officer. There have been no comments from SWAP in their audits of these key systems that have raised fraud alarms.</p>

	<p>There are also strong controls in place around the letting of contracts. Our procurement systems mean that contracts are let through a heavily prescribed process, with a number of trained staff involved and a formal Decision to let the contract</p> <p>From the Anti-Fraud and Corruption report, it is clear that there have been a number of fraud and corruption allegations made that the relevant officers are investigating. Whilst it is disappointing to see that there are cases that need to be investigated, officers have informed me that (i) these cases involve relatively small amounts, (ii) that all cases are actively investigated in line with our policies, and (iii) that in many cases, the initial intelligence has come from members of staff coming forward with our concerns. I understand from the officers that the number of cases is consistent with previous years and not unduly high given the national picture.</p> <p>At the January 2018 meeting, the Audit Committee re-endorsed our policies on fraud and corruption, bribery and money laundering. We operate a “zero tolerance” policy and investigate all allegations We always encourage our staff to come forward with any concerns, such as through the Whistleblowing Policy, and I understand that this has been followed by our staff in some instances in 2017/2018.</p> <p>A further control against fraud is through our budget monitoring. Budget holders and financial staff who are familiar with the services that they support is regularly carried out, and reported back to senior managers monthly and Cabinet quarterly. Any potentially fraudulent activities that would be large enough to impact on the financial statements would be highly visible in this work, and would be investigated. Further, Corporate Finance staff who compile the Statement of Accounts are highly experienced and trained in this task, and do carry out comparative analysis year on year, and any anomalies would be questioned.</p>
<p>What are the results of this process?</p>	<p>I would consider that the risk of material misstatement due to fraud is very low.</p>

What processes do the Council and Pension Fund have in place to identify and respond to risks of fraud?

I would again refer you to the recent Audit Committee paper on the topic, which includes both previous and planned actions in combatting known and emerging fraud risks (such as the proposed new audit on Combatting Tax Evasion and the Criminal Finance Act 2017, included in our Internal Audit Plan for 2018/2019).

Please contact Martin Gerrish directly for any further information on this topic.

<http://democracy.somerset.gov.uk/documents/s5781/Item%209%20-%201%20Fraud%20Jan%202018%20for%20AC.pdf>

In terms of the “3 lines of defence”, our last line is our internal audit function. Audit Committee can place reliance on the work undertaken by SWAP. Their support is set out within the Internal Audit Plan, which is approved annually by the Audit Committee. All auditors will remain vigilant for fraud risks in every audit, and for 2017/2018, the audits that are particularly relevant included:-

- i) The Plan included a full 30 day audit on our 3 largest financial systems – Accounts Payable, Accounts Receivable and Payroll. There was also an audit on SAP IT controls, one on IT Threat Management and 100 days on financial management in schools.
- ii) A specific audit was included for local preparations for managing National Fraud Risks, and the results of this work have informed the 2018/2019 Plan.
- iii) An allowance was made for anti-fraud and corruption support, and SWAP have provided further days during the year on individual cases as they have arisen (with trained, specialist officers being deployed).
- iv) Our Internal Audit Plan is set on a number of key principles, which includes deliberately targeting high risk and high budget areas.

The Pension Fund adopts the same key policies used by SCC in relation to fraud prevention and minimising the risk of fraud. The National Fraud Initiative includes a number of sections on pensions, which are checked by key Peninsula Pensions staff on our behalf.

<p>Have any specific fraud risks, or areas with a high risk of fraud, been identified and what has been done to mitigate these risks?</p>	<p>There are no fraud risks that are “Somerset specific”. As an upper tier local authority, there are a number of fraud risks that we have in common with similar organisations, such as Council Tax and Business Rate frauds, Blue Badges, pensions and payroll, concessionary fares and procurement.</p> <p>(Although Council Tax fraud is not actually perpetrated against the County Council, it is we who stand to lose the most, and therefore we have been proactive in supporting our Districts to investigate).</p> <p>There is a risk that pensioner deaths are not identified in a timely manner and that payments continue. However, periodical mortality screening checks are carried out (covering both the UK and overseas) to identify and recover potential overpayments.</p>
<p>Are internal controls, including segregation of duties, in place and operating effectively?</p>	<p>Yes. The relevant SWAP audit reports continue to provide assurance that adequate division of duties are in place.</p>
<p>If not, where are the risk areas and what mitigating actions have been taken?</p>	<p>The Audit Committee has had a Partial audit on the subject of Debt Management, and takes an active interest in debt recovery. Most of the recommendations were about service actions and processes outside the Accounts Receivable system, and were more concerned with timeliness of referral for legal debt recovery and administrative tasks.</p> <p>Nonetheless, the Audit Committee received a number of reports at the November 2017 meeting, where officers outlined the improvements that they were making to the overall process, and the new Income Code of Practice that the Audit Committee endorsed as a new and mandatory requirement to improve our internal controls.</p>
<p>Are there any areas where there is a potential for override of controls or inappropriate influence over the financial reporting process (for example because of undue pressure to achieve financial targets)?</p>	<p>I am not aware of any instances where management have overridden controls or have tried to influence the financial reporting of the position to achieve financial targets.</p>
<p>Are there any areas where there is a potential for misreporting?</p>	<p>None that I am aware of.</p>

<p>How does the Audit Committee exercise oversight over management's processes for identifying and responding to risks of fraud?</p>	<p>See information above about audit reports received.</p>
<p>What arrangements are in place to report fraud issues and risks to the Audit Committee?</p>	<p>The Anti-Fraud and Corruption Policy sets out the ways to report and investigate fraud. There are a number of ways in which a fraud can be reported and officers or members to whom an allegation could be raised (including myself as Chair).</p> <p>The normal reporting of frauds comes through the Strategic Manager for Financial Governance, who is also the County Council's Anti-Fraud Officer. Should there be fraudulent activity that needs more urgent reporting, I would expect the officer to inform me directly, otherwise there is a verbal update to each Audit Committee and also a formal report annually in January.</p> <p>If a fraud were to impact on the Pensions Fund, I would expect the officers to bring this to the next Pensions Board in addition.</p>
<p>How do the Council and Pension Fund communicate and encourage ethical behaviour of its staff and contractors?</p>	<p>There are many ways in which this is achieved. I understand that the Director of Finance's report will include a response on this topic, but generally this is done through the 4Cs and through positive messages such as the staff awards and successes reported from the Leader and Chief Executive through Our Somerset. For the policy side, we have Codes of Conduct and Standards in both HR and Finance, and there are often communications about policies in Core Brief, which goes to staff monthly.</p> <p>I am told that all of our procurement processes require the bidders to sign and confirm Anti-Collusion declarations. All outside organisations contracted by the Pensions Fund are bound within strict ethical behaviours set out in their contract.</p>
<p>How do you encourage staff to report their concerns about fraud? Have any significant issues been reported?</p>	<p>The Anti-Fraud and Corruption Policy makes it clear that every effort will be made to keep allegations anonymous. The report does not have to be to an officer's line manager if that could be difficult, and many alternatives are set out within the Policy to make reporting easier.</p> <p>Similar provisions are made in the Whistleblowing Policy.</p> <p>No significant issues have been reported in 2017/2018.</p>

<p>Are you aware of any related party relationships or transactions that could give rise to risks of fraud?</p>	<p>No. Officers and members are governed by their respective Codes of Conduct. Members and senior officers are obliged to sign documentation about their interests, and members are required to declare any interests at all relevant meetings.</p>
<p>Are you aware of any instances of actual, suspected or alleged, fraud, either within the Council since 1 April 2017?</p>	<p>The confidential report to the Audit Committee has set out all the allegations that officers are aware of during the year. All of these have been investigated and I understand that a number have been closed without the need to refer the matter to the Police. I am not aware of any other fraudulent allegations other than these cases.</p>

Law and regulation

Auditor Question	Response
What arrangements do the Council and Pension Fund have in place to prevent and detect non-compliance with laws and regulations?	As above – strong anti-fraud and corruption measures, strong procurement controls and contract monitoring, and SWAP as internal auditor. There is also the role of the Monitoring Officer.
How does management gain assurance that all relevant laws and regulations have been complied with?	By employing staff with the relevant professional qualifications, skills and knowledge in the critical posts.
How is the Audit Committee provided with assurance that all relevant laws and regulations have been complied with?	As above. As Chair of the Audit Committee, I would “call in” any area of the County Council if I had doubts about compliance. If an audit only achieves Partial assurance, the relevant officers are obliged to attend a public Audit Committee meeting to provide the necessary assurance that the agree improvement plan is completed, and this remains “open” until this has been done.
Have there been any instances of non-compliance or suspected non-compliance with law and regulation since 1 April 2017?	None that I am aware of.
What arrangements do the Council and Pension Fund have in place to identify, evaluate and account for litigation or claims?	I am told that it is much more likely that the County Council will initiate litigation rather than defend it. I am told that the Director of Finance will respond in relation to individual cases.
Is there any actual or potential litigation or claims that would affect the financial statements?	Officers will assess any outstanding legal cases at year end and determine whether they could impact on our financial statements. They are treated in accordance with prescribed accounting processes to ensure that the accounts reflect any genuine exposure that the County Council may have,
Have there been any reports from other regulatory bodies, such as HM Revenues and Customs, which indicate non-compliance?	None that I am aware of.